THE CASE FOR SPECIFIC PERFORMANCE AS THE PRIMARY REMEDY FOR BREACH OF CONTRACT IN NEW ZEALAND

Fionnghuala Cuncannon*

This article examines the appropriateness of damages as the primary remedy for breach of contract in New Zealand. It argues that the civil law approach to contractual remedies, which gives primacy to performance of the obligation, is superior to New Zealand's common law position, which merely seeks to replace the right to performance with an award of damages. The importance of both the normative and practical impact of the remedial framework is examined in order to demonstrate that specific performance is better able to facilitate commercial endeavours. The three justifications for the primacy of damages in the common law (the historical development, the economic theory of efficient breach, and the concern that specific performance will overburden the administration of justice) are examined but rejected as adequate justification for the common law position. It contends that specific performance should be the primary remedy because it is more consistent with the principles that underlie the law of contract. It also contends that specific performance is more practical because it reduces conflict and promotes efficiency. The recommendation is that any change should be through appropriate legislation.

I INTRODUCTION

Contractual rights are a major form of commercial wealth.[1] The law of contract endeavours to define and protect these rights. The availability of appropriate remedies is important to protect the value of contractual rights. In New Zealand the law of contract has traditionally been developed in accordance with the structure and principles of English common law.[2] Consequently, the main

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1 Daniel Friedmann "The Efficient Breach Fallacy" (1989) 18 J Legal Stud 1, 23.

2 John F Burrows, Jeremy Finn and Stephen Todd *Law of Contract in New Zealand* (2 ed, LexisNexis, Wellington, 2002) 8.

mechanism for protecting contractual rights has been damages for breach of contract. It is the thesis of this article that the law of contract should be revised and specific performance should become the primary remedy for breach of contract in New Zealand.

In common law systems specific performance is an order of the court requiring the defendant to personally perform the promise made.[3] The defendant must actually fulfil the contractual obligation, for example deliver the chattel, or be held in contempt of court. In civil law systems the term is used more broadly and also includes actions to recover the price of having somebody else (including the plaintiff) perform the contract, the cost of curing a defect, or the cost of substitute goods.[4] In cases where only the defendant can perform the contract the court will order them to do so. As in common law jurisdictions if they do not do so they will be fined or imprisoned.[5] This analysis is mainly concerned with the situation where only the defendant can perform the contractual obligation, because it is in these cases that the difference between the common law and civil law approach is of the greatest practical importance.

In New Zealand specific performance is available but is a discretionary remedy. In comparison contractual damages are paid as a matter of right when a breach of contract is established.[6] The discretionary nature of specific performance is due to its historical development, although academic and judicial support for this position has developed based on more pragmatic grounds. Academic support for the primacy of damages has been expressed in the theory of efficient breach which has attempted to explain and justify the common law's preference for damages.[7] Judicial support for the primacy of damages has acknowledged the efficiency arguments but has been more concerned with the burden that supervising specific performance could have on the administration of justice.[8] The historical basis for the primacy of damages, the theory of efficient breach, and the judicial concerns about the practical application of specific performance will be discussed to establish whether they are able to justify the primacy of damages in common law jurisdictions. These justifications are then contrasted with the philosophical and practical advantages of specific performance.

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3 Gareth Jones and William Goodhart *Specific Performance* (Butterworths, London, 1986) 1.

4 GH Treitel *Remedies for Breach of Contract: A Comparative Account* (Clarendon Press, Oxford, 1989) 46.

5 Konrad Zweigert and Hein Kötz *Introduction to Comparative Law* (2ed, Clarendon Press, Oxford, 1992) 509.

6 John F Burrows, Jeremy Finn and Stephen Todd *Law of Contract in New Zealand* (2ed, Lexis Nexis Butterworths, Wellington, 2002) 743.

7 For example Richard Posner *The Economic Analysis of Law* (Little & Brown, Boston, 1972).

8 For example *Co-operative Insurance Society Ltd v Argyll Stores (Holdings) Ltd* [1998] AC 1.

II THE PURPOSE OF THE LAW OF CONTRACT

The law of contract enables individuals to form relationships and deal with their property and other resources in an organised manner consistent with their personal freedom. It balances the needs of the greater community against the personal benefit of the individual. Contracts are also a mechanism for allocating risk. Parties accept the detriment of being bound to their own promises in return for being able to rely on the other party or parties to the contract being bound by their promises. Risk allocation and the certainty risk allocation creates are fundamental to the promotion of commercial activity.[9]

Determining whether damages or specific performance is the more appropriate primary remedy for breaches of contract is not merely a comparative exercise. The availability of a philosophically sound, but pragmatic, remedial framework is as important as the substantive law that governs the contract because remedies give the contractual terms substance. A remedy ensures that the contract is worth more than the paper it is written on, turning normative statements into "living truths".[10] Without an independent and reliable system for developing, awarding, and enforcing remedies a party to a contract with sufficient physical or economic strength would be able to breach with impunity.

The available remedies must be clearly articulated and relevant information readily accessible to the parties. The remedial setting is the backdrop for the formation and performance of the contract and resolution of any disputes arising out of the contract. Matters of price and risk are affected by the remedies available.[11] The remedial backdrop is also important because the ability of parties to choose their own remedies is extremely limited. The parties cannot contract that in the event of breach the contract will be specifically performed. Nor can a contract contain a liquidated damages clause (which provides for damages to be paid by the defaulting party) if the damages which would be payable are so disproportionate to the actual amount of real damage that they are punitive.[12]

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9 Frank Menetrez "Consequentialism, Promissory Obligation, and the Theory of Efficient Breach" (2000) UCLA L Rev 859, 873.

10 Grant Hammond "The Place of Damages in the Scheme of Remedies" in PD Finn (Ed) *Essays on Damages* (The Law Book Company, Sydney, 1992) 192.

11 Richard Craswell "Contract Remedies, Renegotiation, and the Theory of Efficient Breach" (1988) 61 S Cal L Rev 629, 630.

12 Alan Schwartz "The Case for Specific Performance" (1979) 89 Yale LJ 271, 273-4.

III JUSTIFYING THE PRIMACY OF DAMAGES – THE EQUITABLE ORIGINS OF SPECIFIC PERFORMANCE

A History of Specific Performance in the Common Law

The first justification for the primacy of damages in the common law is the historical development of the common law remedial framework. The primacy of damages is part of the heritage of the common law and reflects the competitive relationship between the common law courts and the courts of Chancery.[13]

Specific performance was an exceptional remedy partly because the courts of Chancery had to be careful not to impinge upon the jurisdiction of the common law courts. The courts of Chancery were to supplement, not supplant, the common law courts. Consequently, equity was only to be used when the common law courts were not capable of doing justice between the parties. The courts of Chancery were also reluctant to use contempt of court proceedings to redress private disputes.[14] The courts of Chancery were also concerned that their authority would be undermined if orders could not be enforced and the contempt proceedings were put to the test.[15] These concerns, which continue to resonate with modern jurists,[16] do not adequately explain why this is particularly disturbing in cases of specific performance when in all private litigation there is a threat of contempt of court.[17]

B Equitable Remedy

The equitable origins of specific performance are still relevant in New Zealand. Although New Zealand's courts are not divided into equitable and common law courts, the origin of the action and the remedy determine both availability and application. The most important fetter on equitable remedies is that they are discretionary. The equitable origins of specific performance are also relevant because equitable defences such as unfairness[18] or hardship[19] are available which are not

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13 Treitel, above n 4, 70.

14 Treitel, above n 4, 70.

15 Robert J Sharpe *Injunctions and Specific Performance* (2ed, Canada Law Book Inc, Toronto, 1992) 7-1.

16 For example *Argyll Stores,* above n 8.

17 For further discussion see Part V A 2(d) Critique of the House of Lords' decision.

18 For example in *Attorney-General for England and Wales v R* [2002] 2 NZLR 91 the New Zealand Court of Appeal refused to grant an injunction restraining a former SAS soldier from publishing a book in breach of his employment agreement in part because of the inherent pressure to sign the contract and the fact he was told he could not take any independent advice. The other relevant factors were the lack of mutuality and considerations of freedom of speech.

19 For example in *Patel v Ali* [1984] Ch 283 Goulding J refused to grant specific performance because after the sale of the house the vendor had become disabled and was heavily reliant on her neighbours for assistance which she would lose if forced to move.

available to an action for damages.[20] For example, specific performance will be denied if it would take advantage of another's mistake or it would be unjust to order it.[21]

C The Issue of Adequacy

In New Zealand specific performance will be awarded when damages are inadequate.[22] The test of adequacy of damages was developed to reduce the conflict between the common law courts and the courts of Chancery.[23] The adequacy test is consistent with the principle that equitable remedies were developed to supplement remedies available at common law.

The adequacy test articulates the relationship between common law and equity but it does not explain the role of remedies in giving effect to contractual obligations or the reasonable expectations of the parties. As the historical basis for the adequacy test has been removed by the merging of the common law courts and the courts of Chancery, the availability of remedies should be reconsidered in light of current social and economic expectations of the law of contract. Both the adequacy test and the superiority of damages over specific performance have more recently been defended and affirmed on the basis of economic efficiency and cost effectiveness.

IV JUSTIFYING THE PRIMACY OF DAMAGES – THE THEORY OF EFFICIENT BREACH

A Introduction

Although historical reasons are no longer a sufficient justification for the primacy of damages in the common law, academic support for this approach to remedies has developed based upon the theory of efficient breach. Even though there are many difficulties associated with the calculation of damages, economic theory has been invoked to both explain and justify the common law position. Oliver Wendell Holmes famously wrote, "the duty to keep a contract at common law is a prediction that you must pay damages if you do not keep it, - and nothing else."[24] This can be contrasted with the approach in civil law where a breach does not defeat the promisee's right to receive performance but rather provides them with the opportunity to have their claim for performance supported by the courts.[25] The common law's continuing preference for damages has been justified as more economical than the civil law approach because damages allow the promisor to breach when it is more efficient for them to do so than to perform the contract.

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20 Treitel, above n 4, 46.

21 Jones and Goodhart, above n 3, 10.

22 *Loan Investment Corporation of Australasia v Bonner* [1970] NZLR 724 (PC).

23 Treitel, above n 4, 64.

24 Oliver Wendell Holmes "The Path of Law" (1897) 10 Harv L Rev 457, 462.

25 Charles Szladits "The Concept of Specific Performance in Civil Law" Am J Comp L IV 208, 220-1.

An efficient breach[26] is a wilful breach by one party by either performing the contract with a third party for a greater profit or refusing to perform the contract to avoid loss that would result from that performance.[27] The theory of efficient breach justifies such breaches on the basis that promisors who breach contracts increase society's welfare when the benefit of the breach is greater than the promisee's losses. If a party can compensate the promisee for any loss resulting from the breach and still generate a greater profit they should breach the contract.[28]

B Critique of the Theory of Efficient Breach

The efficient breach theory can be criticised on three grounds. First, it is inconsistent with the normative aims of contract law. Secondly, even if the theory is accepted, it fails to translate into practice because the costs the promisor are expected to weigh in deciding whether a breach would be efficient are rarely as concrete as the examples used when developing the theory. Consequently, in practice the theory perpetuates inefficient breaches. Thirdly, the theory of efficient breach is inconsistent with other areas of law.

1 Normative difficulties with the theory of efficient breach

Economic analysis views contracts as a mechanism to facilitate the exchange of goods and services to where they are valued most. Therefore, if a contract impedes that exchange breach of that contract should be encouraged.[29] This approach is inconsistent with the law's aim of preventing and resolving conflict, the purpose of creating a contract, the intrinsic value of a promise, and the law's concern to prevent people from profiting from their own wrongdoing.

The legal system endeavours to protect reliance and expectation interests in order to reduce conflict. Breaches of contract, irrespective of whether or not they are efficient, lead to disputes. The theory of efficient breach encourages "breach first, talk afterwards".[30] It encourages one party to determine unilaterally the direction of a bilateral relationship. The theory of efficient breach does

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26 For example, an efficient breach occurs when A contracts to build a machine for B for which A will receive a net profit of $10,000. Before A begins building the machine, C requests A to build another machine for which A will receive a net profit of $20,000. A is unable to make both machines but if A breaches with B it will cost B $2,000 above the original cost of the machine to get another manufacturer to perform the original contract. According to the efficient breach theory A should breach the contract with B because even after compensating B, A will be $8,000 better off.

27 Joshua Cender "Knocking Opportunism: A Reexamination of Efficient Breach of Contract" (1995) Ann Surv Am L 689.

28 Craig S Warkol "Resolving the Paradox Between Legal Theory and Legal Fact: The Judicial Rejection of the Theory of Efficient Breach" (1998) 20 Cardozo L Rev 321-322.

29 Menetrez, above n 9, 883.

30 Joseph M Perillo "Misreading Oliver Wendell Holmes on Efficient Breach and Tortious Interference" (2000) 68 Fordham L Re 1085, 1102; Ian R Macneil "Efficient Breach of Contract: Circles in the Sky" (1982) 68 Va L R 947, 968.

not allow for intangible human reactions. It assumes that everybody is a rational economic actor who will be satisfied by an award of damages.[31]

The essential purpose of a contract is the performance of the promises it encompasses. The bargain is made for the performance of the promise, not for a promise and the right to win a lawsuit.[32] Furthermore, in accordance with the principle of freedom of contract, if parties to a contract wish to stipulate that a promisor is allowed to breach subject only to the payment of damages they are free to do so. Parties have the right to be even more specific and could include a liquidated damages clause setting out the damages to be paid on breach.[33]

In contrast, the efficient breach theory undermines the promisee's freedom to determine its contractual relationships because it allows the promisor unilaterally to determine the 'best use' of the promisee's property.[34] This is inconsistent with the parties' motivations for entering into the contract and the principle of freedom of contract.

Furthermore, the provision of remedies for breach does not mean that the law of contract has implied a term into the contract that encourages or justifies breach. The purpose of a remedy is to vindicate a right not to replace it.[35] That a promisee can seek redress through the legal system in no way justifies the promisor's breach.

The theory of efficient breach also undermines the risk allocation function of contracts. If a promisor is able to escape a promise because it is no longer as profitable as it once was, then securing goods or services and planning becomes very difficult.[36]

Promises generate an obligation to make the future conform to a particular description.[37] On an ordinary understanding the making of a promise imposes an obligation to perform the promise. Economic analysis rejects the idea of a moral obligation to keep a promise because the purpose of the legal system is to increase aggregate wealth and not to command obedience to an agreement that

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31 Craig S Warkol, above n 28, 343.

32 Perillo, above n 30, 1094.

33 A liquidated damages clause will be set aside if the amount it provides for is excessively high because it is considered to be punitive rather than compensatory.

34 Friedmann, above n 1, 23.

35 Friedmann, above n 1, 1.

36 Craig S Warkol "Resolving the Paradox Between Legal Theory and Legal Fact: The Judicial Rejection of the Theory of Efficient Breach" (1998) 20 Cardozo L Rev 321, 347.

37 Menetrez, above n 9, 873.

lacks practical utility.[38] However, this approach reduces the legal system to a mere mechanism for setting prices in the form of damages.[39]

The crucial issue is who should benefit from a third party's offer to pay a higher price for the goods or service.[40] The efficient breach theory is objectionable because it attempts to justify why the promisor should attain a benefit through the commission of a wrong (the breach of contract).[41] If any benefit is to accrue, it should be to the original promisee because the realisation of any benefit is dependent upon the contractual rights of the promisee.

It has been suggested that in cases where the cost of full performance is greater than the value of that performance to the promisee the routine grant of specific performance may lead to the promisor having to 'bribe' the promisee to settle the case.[42] This proposition fails to recognise that, where the cost of performance is greater than the value the promisee will accrue, allowing the promisor not to perform results in unjust enrichment of the promisor.[43] A legal system that restricts the availability of specific performance undermines the parties' faith in realising their bargain.[44] Therefore, the law should err on the side of protecting the promisee rather than the promisor.

2 The practical difficulties with the theory of efficient breach

Even if the philosophical difficulties with the theory of efficient breach were overcome or disregarded, the practical application of the theory faces a number of obstacles. The theory of efficient breach is premised on making a profit once the promisee has been compensated. Ensuring that the promisee has been fully compensated is very difficult in practice. The first hurdle is determining the true extent of the loss suffered.[45] If this hurdle is overcome the law of contract contains a number of doctrines which have the effect of preventing the promisee from recovering the full extent of their loss.[46]

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38 Richard Morrison "Efficient Breach of International Agreements" (1994) 23 Denv J Int'l L & Policy 183, 190-1.

39 Friedmann, above n 1, 1.

40 Friedmann, above n 1, 5.

41 Friedmann, above n 1, 6.

42 Anthony Kronman "Specific Performance" (1978) 45 U Chi LR 351, 366-7.

43 Perillo, above n 30, 1103.

44 Friedmann, above n 1, 7.

45 Friedmann, above n 1, 13.

46 Such as the requirement that the loss be foreseeable, that the plaintiff must take reasonable steps to mitigate their loss, and in commercial cases the plaintiff cannot recover for the frustration and stress caused by the breach. In addition the cost of resolving the inevitable dispute is unlikely to be fully compensated.

However, even if the legal system did not inhibit the functioning of the theory of efficient breach in this way, the theory would still be inefficient because of the additional transactions it creates. If the contract was performed the promisee could have negotiated to enter another contract with a buyer willing to pay a higher price. This is one additional transaction. In comparison, if the promisor chooses to breach the contract, there will be at a minimum two additional transactions. First, there will be the transaction with the new buyer. Secondly, there will be the transaction forced upon the original promisee as a result of the breach. It is unrealistic to assume there will be no transaction costs in making the compensation payment. It is likely only to be resolved after negotiation or litigation. It may also lead to a third transaction, a tort action against the new buyer for inducing breach of contract.[47]

Furthermore, there must be doubts as to the ability of the promisor to actually predict the costs that will be generated and determine whether or not a breach is truly 'efficient'. [48] Finally, the theory of efficient breach makes a number of assumptions about the parties' behaviour, such as the assumption they will always sue to recover their loss, which will not necessarily occur, meaning that inefficiencies occur.[49]

3 The theory of efficient breach is inconsistent with other areas of law

The theory of efficient breach is not consistent with other doctrines and remedies available in both contract and other areas of the law of private obligations.

It is incorrect to say that the law of contract wants to encourage efficient breaches as other aspects of the law of contract demonstrate the law's disapproval of breaches of contract. The theory of efficient breach is implicitly rejected by the availability of specific performance, punitive damages, and the rule that a pre-existing obligation cannot be consideration for a new contract with the party to whom the obligation is owed because the promisor is already obliged to perform that obligation.[50] The developing doctrine of economic duress is also inconsistent with the theory of efficient breach.[51] In addition, the rule requiring certainty of damages is relaxed when the breach is wilful.[52] Importantly, contract law already provides for situations where performance should be excused due to intervening events or a significant misapprehension by one or both of the parties through the doctrines of frustration and mistake.

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47 Friedmann, above n 1, 6-7.

48 Friedmann, above n 1, 13.

49 Cender, above n 27, 700.

50 Friedmann, above n 1, 18-20.

51 The doctrine of economic duress is developing: see *Dimskal Shipping Co SA v International Transport Workers Federation* [1991] 4 All ER 871.

52 Perillo, above n 30, 1101.

The theory of efficient breach is inconsistent with the tort of interference with contractual relations.[53] "It is a violation of a legal right to interfere with contractual relations recognised by law if there be no sufficient justification for the interference."[54]

Contractual rights also receive protection against third parties through restitution. If a third party receives the performance promised to another they will be liable in restitution unless they acquired title in good faith for value without notice.[55] The purpose of a restitutionary claim is not to compensate for loss suffered but to transfer any increase in value of the assets to the owner. The owner is the person to whom the law gives the sole right to use the property as he or she thinks fit.[56]

The theory of efficient breach is inconsistent with the concept of good faith because it does not give any weight to the promises exchanged and encourages one party to determine unilaterally the direction of the relationship. The doctrine of good faith is yet to be incorporated into every contract in New Zealand.[57] Rather, it is a developing doctrine; it underpins many aspects of the current law and a wider application has received judicial support. His Honour Justice Thomas has championed a general concept of good faith in both making and performing contracts.[58] His Honour understands good faith as "loyalty to a promise".[59] Promoting "loyalty to a promise" will ensure a high level of international business confidence in New Zealand's commercial environment. It will also better equip New Zealand enterprises to operate in the international commercial arena which, as demonstrated by instruments such as the CISG[60] and Unidroit Principles of International Commercial Contracts,[61] incorporates a duty of good faith. Therefore, the theory of efficient breach is inconsistent with the international commercial environment which New Zealand enterprises operate, or aspire to operate, in.

The theory of efficient breach is a modern justification for the primacy of damages in the common law. It views specific performance as a hindrance to the allocation of resources to the party who values them most. However, the theory must be rejected as sufficient justification for the common law position because it is conceptually flawed and does not work in practice. It does not

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53 Friedmann, above n 1, 20; Perillo, above n 30, 1100.

54 *Quinn v Leathem* [1901] AC 495, 510 (HL) Lord MacNaghton.

55 Friedmann, above n 1, 22.

56 Zweigert and Kötz, above n 5, 583.

57 As it is in America by virtue of section 205 of the Restatement of Contracts, Second.

58 *Livingstone v Roskilly* [1992] 3 NLZR 230 (HC); *Bobux Marketing Ltd v Raynor Marketing Ltd* [2002] 1 NZLR 506 (CA); "An Affirmation of the Fiduciary Principle" [1996] NZLJ 405.

59 *Bobux Marketing Ltd v Raynor Marketing Ltd* [2002] 1 NZLR 506, 516 [41] (CA) Thomas J dissenting.

60 United Nations Convention for the International Sale of Goods 1980, Art 7(1).

61 Unidroit Principles of International Commercial Contracts, Art 1(7).

give adequate consideration to the law's role in preventing and resolving conflict, the purpose of creating a contract, the intrinsic value of a promise, and the law's concern to prevent people profiting from their own transgressions. The theory does not work in practice because promisors will be unable to determine accurately whether or not a particular breach will be efficient. This is compounded by legal doctrines which limit the ability of the promisee to recover fully. However, even if these two obstacles could be overcome, the theory is itself inefficient because it generates more transactions, and therefore related costs, than specific performance. In addition the theory is premised upon the assumption that, as rational economic actors, promisees will not be upset by the promisor being able to unilaterally determine the best use of the promisee's contractual rights. As a result of these internal difficulties and its inconsistency with other interrelated areas of law the theory of efficient breach must be rejected as a justification for the supremacy of damages.

V JUSTIFYING THE PRIMACY OF DAMAGES – PROTECTING THE ADMINISTRATION OF JUSTICE

The primacy of damages in the common law has also been justified on the basis that it is a more practical approach to resolving contractual disputes. This argument is supported by the orthodox position with respect to the differences between the common law and the civil law approaches to specific performance. The orthodox position is that although they may have different starting points the same conclusion is reached in the end – that is, most commercial disputes are resolved through an award of damages.[62] This Part uses *Co-operative Insurance Society Ltd v Argyll Stores (Holdings) Ltd*[63] *(Argyll Stores)* to demonstrate that although this may be true of contracts for the sale of generic goods the outcomes are not always the same. In doing so the weaknesses of the practical concerns, which have justified the common law position, namely the issue of supervision, the limits to personal freedom, unwanted performance, and commercial expectations, are also demonstrated.

A The Issue of Supervision

1 The issue

Difficulty in supervision is not an absolute bar to specific performance but rather one of the factors that must be balanced in determining whether or not it should be granted.[64] Concern has been expressed that specific performance strains the administration of justice because in many cases

62 For example Zweigert and Kötz, above n 5; Treitel, above n 4; Nigel Foster *German Legal System & Laws* (2ed, Blackstone Press, London, 1996).

63 [1998] AC 1.

64 Treitel, above n 4, 69.

it will not be possible for the court to be sufficiently clear what performance is due or to supervise performance adequately.[65]

2 Co-operative Insurance Society Ltd v Argyll Stores (Holdings) Ltd

Currently, the highest common law appellate court decision regarding the availability of specific performance is *Argyll Stores.* In *Argyll Stores* the House of Lords reiterated the common law's continued preference for damages as the primary remedy for breach of contract. A restrictive approach towards specific performance was confirmed by their Lordships because of the potential strain on the administration of justice. The relevance of this decision to New Zealand was confirmed by the New Zealand Court of Appeal in *Attorney-General for England and Wales v R.*[66]

(a) The facts

Argyll leased the largest unit in a shopping centre from Co-operative Insurance for 35 years from August 1979. The lease included covenants obliging Argyll to use the premises as a supermarket and to keep the premises open for retail trade during normal business hours. The lease also enabled Argyll to assign it. In 1995, having suffered a substantial loss the previous trading year, Argyll gave notice that it intended to close the supermarket. Co-operative Insurance responded by asking Argyll to keep the store open until a suitable assignee could be found and offered a temporary rent reduction because it was concerned about the effect the closure would have on the other stores in the shopping centre. The supermarket was the anchor tenant and its prolonged closure would lead to fewer customers at the shopping centre and a corresponding reduction in the level of rents Co-operative Insurance could charge other tenants. Argyll did not respond to this request and instead stripped the supermarket of its fixtures and fittings and immediately closed the supermarket. Co-operative Insurance immediately commenced proceedings for specific performance and/or damages. It was estimated that the cost of refitting the supermarket would exceed £1 million.

In the summary proceedings Judge Maddock granted an order for damages. An order for specific performance was refused on the basis that it was long-standing practice that damages were the appropriate remedy for a breach of a keep-open covenant and Argyll would incur vastly disproportionate costs if ordered to re-open the supermarket.

(b) The Court of Appeal's decision

The English Court of Appeal (Leggatt and Roch LJJ, Millett LJ dissenting) allowed Co-operative Insurance's appeal and granted specific performance. Leggatt LJ was of the opinion that an award of damages would be unlikely to compensate Co-operative Insurance fully and in

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65 Jones and Goodhart, above n 3, 2.

66 [2002] 2 NZLR 91,120 Tipping J (CA).

particular the losses of the other tenants would not be recoverable unless they were reflected by a reduction in rent. Furthermore, any costs involved in reopening the store were due to Argyll's failure to respond to Co-operative Insurance's letter. Argyll had acted with "great commercial cynicism" rather than keeping "an unambiguous promise".[67]

Roch LJ was also of the opinion that specific performance should be granted because damages would be an inadequate remedy.[68] Argyll's obligations were sufficiently well defined and day-to-day supervision by the court would not be necessary.[69] Importantly, Roch LJ found it "inconceivable" that Argyll would not run the store efficiently if ordered to reopen. Furthermore Argyll had acted "wantonly and quite unreasonably" in removing the fixtures and fittings without answering Co-operative Insurance's letter.[70]

Millett LJ dissented on the basis that ordering a business to remain open had the potential to expose the promisor to "potentially large unquantifiable and unlimited losses which may be out of all proportion to the loss which his breach of contract has caused".[71] Millett LJ was of the opinion that specific performance should only be granted if it is appropriate to do so. The inadequacy of damages would be one factor in determining whether specific performance was appropriate but the potential effect on the defendant must also be considered, since equitable remedies are an instrument of justice and must be refused when there is the potential that they will become "instruments of oppression".[72]

The order for specific performance was suspended for three months to allow Argyll to complete an assignment of the lease to another supermarket chain.[73]

(c) The House of Lords' Decision

Despite the order for specific performance never coming into effect (because of the assignment) the House of Lords reversed the Court of Appeal's decision. Their Lordships were of the opinion that the practice of not ordering specific performance where there is an agreement to carry on a business is not based on the inadequacy or otherwise of damages but rather due to the concern that

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67 *Co-operative Insurance Society Ltd v Argyll Stores (Holdings) Ltd* [1996] 3 All ER 934, 940 (CA).

68 *Argyll Stores*, above n 67, 941 (CA).

69 *Argyll Stores*, above n 67, 943 (CA).

70 *Argyll Stores*, above n 67, 943 (CA).

71 *Argyll Stores*, above n 67, 948 (CA).

72 *Argyll Stores*, above n 67, 949 (CA).

73 *Argyll Stores*, above n 8, 9 Lord Hoffmann (for the court) (HL).

courts would be inappropriately involved in the supervision of the order. The cost of supervising the performance of the contract through "an indefinite" series of rulings was undesirable.[74]

Furthermore, their Lordships were concerned that contempt of court proceedings are too powerful to be a suitable mechanism for resolving private disputes.[75] First, the threat of contempt proceedings requires the promisor to run a business they do not think is commercially viable, under the threat of breaching the court order. Secondly, the seriousness of a finding of contempt of court will mean the litigation is drawn out and expensive.[76]

Lord Hoffmann drew a distinction between orders requiring the performance of an activity and orders requiring a result to be achieved. His Lordship was of the opinion that in the case of orders requiring a result, even if they require a complicated process to be achieved, the court is only called upon to judge the final result meaning the supervision objection is of no concern. This distinction explained why the courts have in the past awarded specific performance of building contracts and repair covenants.[77]

However, even in cases where a result is desired, an order for specific performance should not be made where the order cannot be formulated with sufficient precision. If the order lacks precision, the same expensive litigation will arise because the court will be required to clarify matters. Otherwise the promisor will unfairly incur additional expenses through over-compliance.[78] That a contract is sufficiently certain for the purposes of contract formation does not necessarily mean that the terms are precise enough to be specifically performed.[79]

Lord Hoffmann was of the opinion that the clause in the contract between Argyll and Co-operative Insurance requiring the store to remain open was not sufficiently definite because it did not specify the level of trade or the area of the premises in which trade must be conducted.[80] The way the promisor previously performed the promise cannot be the measure of the obligation under the contract.[81]

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74 *Argyll Stores*, above n 8, 12 Lord Hoffmann (for the court) (HL).

75 *Argyll Stores*, above n 8, 12 Lord Hoffmann (for the court) (HL).

76 *Argyll Stores*, above n 8, 13 Lord Hoffmann (for the court) (HL).

77 *Argyll Stores*, above n 8, 13 Lord Hoffmann (for the court) (HL).

78 *Argyll Stores*, above n 8, 13 Lord Hoffmann (for the court) (HL).

79 *Argyll Stores*, above n 8, 14 Lord Hoffmann (for the court) (HL).

80 *Argyll Stores*, above n 8, 16 Lord Hoffmann (for the court) (HL).

81 *Argyll Stores*, above n 8, 17 Lord Hoffmann (for the court) (HL).

His Lordship was also of the opinion that it is not wise of the courts to make somebody carry on a business at a loss if there is a viable alternative for compensating the promisee.[82] An award of damages brings the conflict to an end, allowing the parties to "heal their wounds" without the "yoke of a hostile relationship".[83]

Lord Hoffmann rejected the argument that if the order became oppressive it could be varied or discharged on application by the promisor on the grounds that an order would be a final order which could only be discharged where the injuncted activities had been legalised by statute. Even if there was jurisdiction to discharge an order because of a change in circumstances which made it oppressive, the potential for oppression would have been entirely predictable at the date the order. Accordingly, there would have been no changed circumstances sufficient to warrant the discharge of the order.[84]

(d) Critique of the House of Lords' decision

The decision of the House of Lords raises a number of legitimate concerns about how specific performance works in practice. However, their Lordships' approach to resolving these concerns was unduly narrow and failed to draw on the experiences of civil law jurisdictions that have already addressed these issues. Their first concern was that an order to keep the store open would lead to multiple applications to resolve issues concerning the quality of the performance. In *Argyll Stores* this was irrelevant because the contract had in fact already been assigned. If there is the potential that an award of specific performance will give rise to continuous applications to the courts this should be established and weighed in each case.[85] Berryman has suggested that it is best to adopt a "wait and see" approach. The decree of specific performance should be granted and if the feared multiple actions arise the court can revert to damages to bring finality to the dispute.[86]

The experience of the German courts also casts doubt on the extent of the supervision issue. Creditors in Germany tend only to bring claims for specific performance when their interest in performance is not easily compensated by money. But if performance is possible and the creditor elects performance, the courts are bound to order specific performance.[87] The primacy of specific

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82 *Argyll Stores*, above n 8, 15 Lord Hoffmann (for the court) (HL).

83 *Argyll Stores*, above n 8, 16 Lord Hoffmann (for the court) (HL).

84 *Argyll Stores*, above n 8, 18 Lord Hoffmann (for the court) (HL).

85 Andrew M Tettenborn "Absolving the Undeserving: Shopping Centres, Specific Performance and the Law of Contract" (1998) Conv & Prop Law 23, 31.

86 Professor Jeff Berryman "Recent Developments in the Law of Equitable Remedies: What Canada Can Do For You" (Paper presented to the New Zealand Centre for Public Law, Victoria University of Wellington, 1 August 2001) 26.

87 Zweigert and Kötz, above n 5, 507.

performance, adopted in the Bürgerliches Gesetzbuch (German Civil Code) in 1900, has not led to German contract law being unworkable, the German courts being overburdened, or to litigation being unduly delayed.

Furthermore, in a commercial situation two factors will help ensure that only proper applications are brought before the court. First, the cost of litigation and the ability of courts to award costs will discourage inappropriate applications.[88] Secondly, the parties will be discouraged from being unduly adversarial because of the adverse effect prolonged litigation will have on their reputations and where applicable the confidence of investors. Reputation is the most important non-legal control of breaches of contract. Breaching contracts and a litigious approach to conflict resolution can affect both the possibility of repeat business and the level of new business through inter-consumer information exchange.[89]

Their Lordships were also concerned that contempt proceedings were too powerful a tool to be used to resolve private disputes. This concern, which echoes that of the courts of Chancery, fails to appreciate that in all matters between two private citizens, whether the proceedings are before the Family Court, the Environment Court, or the High Court, the court's ultimate sanction for breach of its orders is to the hold the perpetrator in contempt of court. If the "spectre" of contempt of court is too powerful a tool when resolving contractual disputes, it must be similarly inappropriate to use it in other disputes between private parties.

The concern that the promisor will be forced to run a business which they have already determined is uneconomical also fails to appreciate the nature of an order for specific performance. In cases such as *Argyll Stores* the order will operate to ensure that the promisor fulfils the obligation they undertook to assign the lease if they did not want to personally fulfil the contract for the full term. Argyll had undertaken the risk of finding a suitable assignee. This allocation of risk would have been reflected in the "price" of the contract. Alternatively, the promisor will negotiate with the promisee to vary or cancel the contract. The most a defendant would be willing to pay in post-breach negotiations is the cost of ending the contract. In cases where the defendant has the power to assign the contract the cost of assigning the contract will be the most they will be prepared to 'pay' the plaintiff to cancel the contract.[90]

The related concern that the order may not be obeyed and that the courts will be brought into disrepute if their orders to specifically perform are not complied with does not account for the

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88 Tettenborn, above n 85, 31.

89 Thomas S Ulen "The Efficiency of Specific Performance: Toward a Unified Theory of Contract Remedies" (1984) 83 Michigan L Rev 341, 347.

90 Tettenborn, above n 85, 35.

importance of reputation. In the context of business relationships the importance of reputation will ensure that, except in the most extreme cases, the courts' orders will be complied with.[91]

The House of Lords made two distinctions which are of questionable value. The first distinction was between cases where a result is required and cases which require the performance of an activity. This distinction was extremely pragmatic as it distinguished the building cases, where specific performance has been awarded, from the case before the Court. The distinction is not sound in practice. Although different activities, the level of detail and co-operation required to complete a building and operate a supermarket are unlikely to be markedly different. There is the same potential for conflict about the details of the operation and the same need for interim injunctions, albeit in building cases this may be over a shorter time frame (in which case Berryman's "wait and see" approach remains the most appropriate). In either situation the potential for repeat applications should be one factor in determining whether or not specific performance is appropriate. This should be determined on a case-by-case basis.

The second distinction made by their Lordships was the distinction between sufficient certainty for the purposes of contract formation and the level of precision required for the order of specific performance. Clause 4(19) of the contract required Argyll "To keep the demised premises open for retail trade during the usual hours of business in the locality and the display windows properly dressed in a suitable manner in keeping with a good class parade of shops." Clause 4(12)(a) specified that the user of the premises was "Not to use or suffer to be used the demised premises other than as a retail store for the sale of food groceries provisions and goods normally sold from time to time by a retail grocer food supermarkets and food superstores." Lord Hoffmann held that these were not sufficiently precise to be the basis of an order of specific performance.

The basis for the distinction between the level of certainty required for contract formation (the basis upon which damages would be awarded) and the level of precision required for an order of specific performance was connected to the concern that multiple actions would be required to determine the promisee's obligations. The conceptual difficulty with this distinction is that if the promisee's obligations are not sufficiently clear when examined by a reasonable person there is no contract. However, if objectively there is a contract it must be clear to a reasonable person what the promisee's obligations are. In practice their Lordships' concern will be dealt with in one of two ways. First, the importance of maintaining a professional enterprise will ensure that the promisee will perform. Secondly, even if they do not maintain a professional enterprise Berryman's "wait and see" approach should be adopted. If and when a problem does arise the Court can deal with this by ruling as to the extent of the promisee's obligations or, if necessary, bringing the proceedings to an end and awarding damages. If plaintiffs in building cases are entitled to specific performance,

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91 Ulen, above n 89, 349.

taking the risk that certain obligations within the contract will only sound in damages, there is no reason why the same rule should not apply to 'keep open' covenants.[92]

The idea that an award of damages allows the parties to rid themselves of the 'yoke of litigation' and 'heal their wounds' fails to recognise that damages do not necessarily compensate a promisee for the harm suffered. Consequently they are left to 'heal' their own wounds while the promisor, who was responsible for causing the harm, is able to move on without being fully held to account. The concept of the 'yoke of litigation' is also unrealistic when the dispute is between two commercial parties. The contract between the tenant and the landlord does not require day-to-day contact or a high level of trust. Argyll was not going to be forced to have a personal relationship with Co-operative Insurance.

Furthermore, it is also important to acknowledge that Argyll was the anchor tenant in the shopping complex. The anchor tenant has "consumer drawing power" which is attractive to smaller tenants who are able to benefit from the increased number of potential customers. The smaller tenants pay a premium through higher rents for this benefit while the anchor tenant receives a corresponding reduction in their rent.[93] Argyll's role as anchor tenant would have been reflected in the contractual terms. The importance of its role as anchor tenant, to both Co-operative Insurance and the other tenants, was not disputed by Argyll. Although the interests of the other tenants are not strictly before the Court there is no reason why their interest in performance should not be considered in determining whether or not specific performance is appropriate.[94]

Lord Hoffmann's opinion that final orders cannot be varied or discharged when circumstances change is doubtful because the courts already have the power to vary orders for specific performance where performance becomes impossible due to the promisee's default.[95] Furthermore, there is nothing to prevent a court, when framing the order for specific performance, from giving leave to the parties to apply for the order to be discharged or varied.[96]

Alternatively, it is possible that if circumstances changed sufficiently the doctrine of frustration would apply. If the contract became oppressive or impossible then the promisee could rely upon the doctrine of frustration which would be a complete defence to an order to specifically perform the contract. In *Johnson v Agnew*[97] the House of Lords held that the non-performance of a specific performance decree was a continuing breach which entitled the promisee to bring a common law

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92 Tettenborn, above n 85, 31.

93 Berryman, above n 86, 23.

94 Tettenborn, above n 85, 34.

95 *Sudaghar Singh v Nazeer* [1979] Ch 474.

96 Tettenborn, above n 85, 38.

97 [1980] AC 367.

action for breach.[98] In such a case the promisee would then be entitled to damages. Surely it is more appropriate for the promisee, rather than the court, to decide whether or not to accept that risk.

Finally, although parties are not able to contract to ensure the contract is specifically performed in the event of breach, they could contract to have damages as the only remedy.[99] This would not need to be a liquidated damages clause but a simple declaration that the parties in the event of breach request the arbitrator or courts to assess damages rather than ordering specific performance.

3 Is there really a problem?

The concern that the courts will not be able to effectively supervise performance and that specific performance will create further litigation is undermined by the success of the courts in supervising complex matters, such as civil rights and competition cases, over long periods of time.[100]

Furthermore, difficulty in determining whether or not the promisor has adequately performed the contract is an unconvincing reason for the court refusing to award specific performance because the same issue is consistently raised in claims for damages. Assessing the performance received in relation to the promises made is no more difficult in a claim for performance than in a claim for damages.[101]

Judges will be required to spend longer formulating the required orders.[102] However, this increase should be more than offset by the saving of not having to calculate damages. Another way of resolving this concern would be to adopt the German approach to the phrasing of orders. A plaintiff is required to set out with sufficient precision his or her demand.[103] The Court will not grant anything the plaintiff has not requested, [104] although they can of course grant less or nothing at all. This puts the onus of formulating the claim, and subsequent order, on the plaintiff who is seeking specific performance.

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98 Berryman, above n 86, 25.

99 *Argyll Stores*, above n 67, 940 Leggatt LJ.

100 Schwartz, above n 12, 293.

101 Zweigert and Kötz, above n 5, 521.

102 Schwartz, above n 12, 293.

103 Zivilprozessordnung (German Code of Civil Procedure), s 253(11) No 2.

104 Zivilprozessordnung (German Code of Civil Procedure), s 308(1).

B Personal Freedom

Specific performance is also criticised for imposing "unduly onerous personal obligations" on the defendant when the plaintiff would be sufficiently compensated by an award of damages.[105] At common law, specific performance will be denied in cases of contracts for service "lest they [the courts] should turn contracts of service into contracts of slavery."[106] There is concern that specific performance may amount to an undue interference with the personal freedom of the defendant especially when the performance can only be provided by personal performance.[107]

The concern that the promisor's liberty will be unjustifiably encroached upon is overstated. In all cases requiring the delivery of goods or in the case of services to be provided by a large corporation a decree of specific performance does not interfere with a person's or corporation's right of association. In the case of an individual performing personal services the loss of liberty argument is much stronger.[108] For this reason, legal systems in which primacy is given to specific performance do not order specific performance unless the act "depends exclusively on the will of the debtor."[109] This does not include cases where a high level of personal skill or creativity is required.[110] For example, a composer will not be ordered to write music; nor will a law professor be required to write a legal commentary. Orders for specific performance are also not available in purely personal matters. Even though the promisor entered into the contract of their own volition these exceptions are justified on the basis of public policy.[111] However, an order for specific performance is still available if fulfilling the contractual obligation requires the co-operation of the promisor's employees or children as the promisor has direct influence over them.[112]

A corollary of the concern that the promisor's liberty will be unjustifiably encroached upon is the concern that an order of specific performance may also create an unjust balance of power between the parties. If the loss the promisor will suffer as the result of the order will significantly outweigh the benefit to the promisee in receiving the performance of that promise, the promisee is put in a position where they can negotiate the release of the promisor from their contractual obligations at a far higher value than the value of the performance.[113] In the colourful language of

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105 Jones and Goodhart, above n 3, 2.

106 *De Francesco v Barnum* (1890) 45 ChD 430, 438 Fry LJ.

107 Treitel, above n 4, 47.

108 Schwartz, above n 12, 297.

109 Zivilprozessordnung (German Code of Civil Procedure), s 888.

110 OLG Frankfurt OLGE 29, 251 reported in Zweigert and Kötz, above n 5, 509.

111 BGH, BGHZ 97, 372.

112 Zweigert and Kötz, above n 5, 508.

113 *Argyll Stores*, above n 8, 15 Lord Hoffmann (for the court) (HL).

Lord Westbury LC, the court must not "deliver over the defendants to the plaintiff bound hand and foot, in order to be made subject to any extortionate demand that he can possibly make."[114] Contractual remedies influence whether or not a party will breach their contract[115] and determine the parties' post-breach bargaining status.[116] The issue is determining the most appropriate balance between the promisee and the promisor. If damages are the primary remedy the promisee is put in a very disadvantageous position. Due to the cost of litigation and other mechanisms which prevent full recovery they are unlikely to be able to be truly compensated. Consequently, they may choose not to enforce their rights or to accept a low settlement offer believing they are making the best of a bad situation. If the choice is between putting the promisee or the promisor in a stronger post-breach bargaining position the promisee should be protected. Both normative concerns and common sense support the role of specific performance in protecting the promisee. The 'innocent' promisee surely has a greater moral claim to protection. Common sense suggests that the remedy which will give the breacher greater reason to pause will reduce the occurrence of breaches.

C Unwanted Performance

Even within a system that promotes performance of contractual obligations there must be some limits on when contracts should be performed. The preceding discussion addressed the situation where the promisee wants to receive the promised performance. Different considerations arise in the case where it is the promisee who wishes to terminate the contract because they have no need of the item to be produced or service to be rendered. So long as the seller is compensated for the profit they would have realised from the contract (subject to mitigation) there is no issue of unfairness. A buyer who terminates the contract is not doing so in an attempt to realise an unexpected benefit. They are merely minimising their own loss while ensuring the seller still receives the benefit they would have received if the contract had actually been fulfilled.[117] This approach resolves the issue raised in *White & Carter (Councils) Ltd v McGregor*[118] where the seller proceeded with unwanted performance over a period of three years, and then claimed the price due under the contract, even though the buyer had attempted to cancel the contract on the same day it was made.

Unwanted performance, which the seller has no special interest in performing other than the financial profit the transaction will generate, should be prevented and the seller restricted to

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114 *Isenberg v East India House Estate Co Ltd* (1863) 3 De GJ S S 263, 273.

115 Richard Craswell "In That Case What is the Question? Economics and the Demands of Contract Theory" (2003) 112 Yale LJ 903, 907.

116 Craswell, above n 11, 640.

117 Friedmann, above n 1, 9.

118 1962 SC (HL) 1.

claiming damages.[119] Article 9:101(2) of the Principles of European Contract Law provides for this situation:

> Where the creditor has not yet performed its obligation and it is clear that the debtor will be unwilling to receive performance, the creditor may nonetheless proceed with its performance and may recover any sum due under the contract unless:
>
> (a) it could have made a reasonable substitute transaction without significant effort or expense; or
>
> (b) performance would be unreasonable in the circumstances.

This is also dealt with in article 649 of the Bürgerliches Gesetzbuch (German Civil Code) which provides that the buyer can terminate the contract so long as they pay compensation to the seller. Where the benefit one party will receive under the contract is purely financial profit, damages will fully compensate them for the premature termination of the contract. A restriction on their ability to claim performance in which they have no legitimate interest is a valid check in any system which has specific performance as the primary remedy for breach.

D Commercial Expectations

Specific performance has also been resisted as being contrary to the reasonable commercial expectation of the parties. The primacy of damages has been justified as reflecting what the parties would have done. When the subject of the contract is unique, so damages would be inadequate compensation, it is appropriate to award specific performance because the parties to a contract would themselves reasonably expect to do that if required to put such a clause in the contract. Consequently, the default position of the law can be justified because it meets the reasonable expectations of contracting parties and is more efficient because the clause does not need to be negotiated.[120] By reflecting normal commercial expectations the law allows the breaching party to make the most efficient use of the resources available to them.[121]

Another reason why specific performance has been resisted is because judges neither have the necessary skills nor the knowledge to second-guess business decisions. An order of specific performance could perpetuate loss-making activities and ultimately affect society's economic well-being, in particular if repeated applications to the court are necessary to enforce the order.[122]

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119 Scottish Law Commission "Report on Remedies for Breach of Contract" (Scott Law Com No 174, Edinburgh, 1999) 4.

120 Anthony Kronman "Specific Performance" (1978) 45 U Chi LR 351, 365.

121 Jones and Goodhart, above n 3, 2.

122 Hwee Ying Yeo "Specific Performance: Covenant to Keep Business Running" (1998) JBL 254, 256.

The concerns about common practice and commercial expectations, such as those expressed above and by Millett LJ,[123] are not good arguments for retaining a restricted approach to the availability of specific performance. They merely demonstrate that the appropriate method of change is legislation. Hammond's recommendation of a short code setting out New Zealand's remedial framework is a sensible method of reform.[124] A short code establishing the principles and availability of specific performance would enable the legal and commercial communities to adjust. New Zealand has enacted such legislation without undue difficulty in the past.[125] Furthermore there is a wealth of models and experience, including the CISG and the Bürgerliches Gesetzbuch (German Civil Code), to draw upon. In particular the code should stipulate that the parties are free to nominate damages as their preferred remedy and that the courts are able to vary or discharge the award if subsequently the contract becomes impossible to perform.[126]

VI THE ADVANTAGES OF SPECIFIC PERFORMANCE

This section evaluates the arguments that underpin the claim that specific performance should be the primary remedy for breach of contract in New Zealand. These include that specific performance gives greater weight to the value of the parties' promises, increases freedom of contract and party autonomy, and gives greater effect to New Zealand's international obligations. Specific performance is also a more practical remedy because it reduces conflict more effectively than damages and promotes efficiency.

A The Philosophical Advantages of Specific Performance

1 The value of a promise

A legal system that imposes strict limitations on the availability of specific performance undermines the parties' trust in the contract.[127] When people enter into a contractual relationship it is with the expectation that the other party will fulfil the promises they made.[128] Ordering specific performance for breach of contract vindicates the promisee's decision to enter into the contract. It vindicates both the trust the promisee placed in the other party and their use of a contract. Individual breaches are unlikely to undermine the contractual institution. However, allowing breaches to be 'bought', as advocated by the efficient breach theory and any system that restricts

123 *Argyll Stores*, above n 67, 950 (CA).

124 Hammond, above n 10, 228.

125 For example, the Contracts (Privity) Act 1982.

126 For example pursuant to section 767 of the Zivilprozessordnung (German Code of Civil Procedure) the original order granting specific performance can be declared to be unenforceable (in whole or in part) if the contract is impossible to perform.

127 Friedmann, above n 1, 7.

128 Zweigert and Kötz, above n 5, 504.

performance-based remedies, undermines the integrity of a system premised upon the free exchange of reciprocal obligations for mutual gain. If people cannot rely on their contracts, or the legal system to vindicate their contracts, they will have to create additional, alternative mechanisms to ensure they can rely on the agreement. Such mechanisms could include the parties making good faith deposits or performance bonds with a third party which in the event of breach are paid to the promisee. Such bonds are used in the building industry to protect subcontractors.[129]

2 Supporting freedom of contract and party autonomy

Specific performance is the best method of compensating a promisee for breach of contract because it gives the exact performance bargained for.[130] Equally the promisor is only required to do what they freely promised to do. In this way specific performance supports the principle of freedom of contract because it merely requires effect to be given to the parties' own declarations of will. Furthermore, specific performance best protects the promisee's subjective valuation of the performance of the contract.[131] When damages are assessed the promisee's expectations are disregarded and instead the 'fair' market valuation of the performance is awarded.[132] Specific performance also supports freedom of contract in this way because the parties' own determination of value is respected and is not later artificially constructed by the court.

Specific performance is also consistent with the principle of party autonomy because it empowers the promisee to determine whether performance of the contractual obligations, although delayed, is still the best mechanism for remedying the breach. It should be the promisee's choice to risk defective performance of the contract.[133] Although damages will in many situations satisfy the promisee's interest in performance, it is unsatisfactory that in common law systems the court determines what the promisee's best interests are. The fact that a promisee is seeking performance, with the inherent risk of further delay and defective performance, demonstrates the promisee's belief that damages are in fact inadequate. The mere fact that the court disagrees with this assessment should not, by itself, justify rejection of the claim.[134]

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129 Ulen, above n 89, 349.

130 Schwartz, above n 12, 274.

131 Ulen, above n 89, 366.

132 PS Atiyah *An Introduction to the Law of Contract* (5 ed, Clarendon Press, Oxford, 2000) 431.

133 Schwartz, above n 12, 304.

134 Zweigert and Kötz, above n 5, 521.

3 Consistency with International Law

The theoretical divide between the civil law and the common law approach to performance remains a serious impediment to the unification of international sales law.[135] The United Nations Convention for the International Sale of Goods (CISG) adopts the general civil law principle that the non-breaching party is entitled to require performance. Importantly, specific performance is not excluded when the non-breaching party could have entered into a substitute transaction although failure to do so may amount to a failure to mitigate under Article 77. The only consequence for a failure to mitigate under the CISG is a reduction in damages, which is not applicable to the right to require performance.

Under the CISG the general principle is that the aggrieved party may require performance of the contract unless they have resorted to a remedy that is inconsistent with a claim for performance. An example of behaviour that is inconsistent with performance would include declaring the contract avoided due to a fundamental breach[136] by the other party.[137] If the seller delivers goods that are not in accordance with the contract the buyer can only require substitute goods if the variation between the goods delivered and the contractual specifications amounts to a fundamental breach and they make a formal request for substitute goods to be delivered.[138]

Article 46(3) of the CISG provides: "If the goods do not conform with the contract, the buyer may require the seller to remedy the lack of conformity by repair unless this is unreasonable having regard to all the circumstances." Whether specific performance is available depends on the law of the country in which performance is sought pursuant to Article 26. If specific performance is not available then Article 46(3) is only relevant to the calculation of damages.

The Sale of Goods (United Nations Convention) Act 1994 (the Act) came into force on 1 October 1995.[139] It enacts the CISG as a code in New Zealand with respect to contracts for the international sale of goods to which it applies.[140] Even though the CISG emphasises the importance of performing the contract, because Article 28 permits the approach of the domestic legal system to be applied, New Zealand's courts are not bound to order specific performance but can continue to apply the adequacy test. Although New Zealand's courts are not bound to order specific performance it is more appropriate to do so because of the emphasis on performance in the CISG.

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135 Zweigert and Kötz, above n 5, 520.

136 Defined in Article 25 as a breach that "…results in such detriment to the other party as substantially to deprive him of what he is entitled to expect under the contract…".

137 The seller has the right to avoid pursuant to Article 49(1) and buyer pursuant to Article 64.

138 Article 46(2).

139 Reg 2 Sale of Goods (United Nations Convention) Act Commencement Order 1995 (SR 1995/168).

140 Sale of Goods (United Nations Convention) Act 1994, s 5.

B The Practical Advantages of Specific Performance

1 Specific performance reduces conflict

The frequency of breach will be reduced where specific performance and restitution are provided because the promisor has less, if anything, to gain from breach.[141] Consequently, the resources required to resolve breaches will be reduced.

Specific performance also fosters bargaining.[142] Resolving problems post-breach is very expensive.[143] Therefore it is better to have as the primary remedy a mechanism which encourages negotiation before a breach occurs. Where the promisor has received a better offer they can use the additional profit they will make to 'purchase' the promisee's consent to a variation or termination of the original contract.[144] As negotiation is less adversarial than litigation the level of conflict is still further reduced.

2 Specific performance is the most efficient remedy

The remedy that will achieve the greatest efficiency in the exchange and breach of contractual obligations is specific performance.[145] The number of cases in which damage awards are unable to fully compensate the promisee outnumbers the number of cases in which specific performance is granted. Therefore, the rationale for the intervention of contract law supports the use of specific performance.[146] If a promisor is not liable for the social costs of the breach they have an inefficiently stronger incentive to breach.[147] In comparison, if parties are aware that their contract will be specifically enforced they will have a strong incentive to efficiently allocate the risks associated with the contract during its formation.[148]

Transaction costs, in particular contract negotiation costs, will be lower if specific performance is the routine remedy for breach of contract. Those who place a high subjective value on the performance of the contract will not need to negotiate in order to avoid the inadequacy of contract damages nor be subject to the cost of proving the inadequacy of damages in court. Those who would

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141 Friedmann, above n 1, 7.

142 Macneil, above n 30, 960.

143 Macneil, above n 30, 968-969.

144 Ulen, above n 89, 373.

145 Ulen, above n 89, 343.

146 Schwartz, above n 12, 275.

147 Linda Curtis "Damage Measurements for Bad Faith Breach of Contract: An Economic Analysis" (1986) 39 Stan L Rev 161, 170.

148 Ulen, above n 89, 365.

prefer damages will be able to inexpensively nominate damages in a standard form remedial clause.[149]

Litigation costs will be reduced because there will be fewer disputes. The difficult evidential issues that currently require determination when trying to claim that damages are unique will not arise.[150] With specific performance the court's factual enquiries stop as soon as it has been determined that a breach has occurred. This eliminates the need to hear evidence on the calculation of damages.[151] The parties can then resolve the issue of the breach by negotiating a settlement or by performing the contract. In this way an award of specific performance is, like an injunction, an ultimatum to the promisor – perform your promise or negotiate to resolve the dispute.[152]

VII CONCLUSION

In New Zealand the primary remedy for breach of contract is damages. Specific performance is a discretionary remedy available when damages are 'inadequate'. The historical basis for the common law approach to damages and the adequacy test are not relevant to New Zealand's commercial environment. Despite this, two additional justifications have been accepted for maintaining damages as the primary remedy for breach of contract in common law legal systems.

The first modern justification is the theory of efficient breach. This theory has been developed by academics to both explain and justify the primacy of damages in the common law remedial framework. The civil law's preferences for specific performance is rejected as inefficient because parties are bound to fulfil their contractual obligations irrespective of the more attractive supervening opportunities. Efficient breach theory is premised upon increasing the aggregate wealth of society by facilitating the most efficient use of resources. Despite this laudable ambition, the theory is conceptually flawed because it gives no weight to the normative value of the law. It fails to account for the legal system's role in preventing and resolving conflict, the purpose of creating a contract, the intrinsic value of a promise, and the law's concern to prevent people from profiting from their own wrongdoing. Furthermore, the theory of efficient breach does not work in practice because it is very difficult to determine accurately the costs that will be incurred if the promisor breaches and therefore the promisor is unable to make an informed decision about whether or not the breach will actually be efficient.

In addition the legal system prevents the theory of efficient breach working in practice because of doctrines that limit the promisee's ability to recover the full extent of their loss. However, even without the operation of these doctrines the theory is in itself inefficient because it creates additional

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149 Ulen, above n 89, 378-379.

150 Ulen, above n 89, 379.

151 Ulen, above n 89, 384.

152 Ulen, above n 89, 399.

and unnecessary transactions. Finally, the theory of efficient breach assumes that parties are rational economic actors who will accept the operation of the theory. Due to these difficulties and its inconsistency with other intersecting areas of law (including other aspects of contract law, torts, restitution and the doctrine of good faith) the theory of efficient breach as a justification for perpetuating the supremacy of damages in common law systems must be rejected.

Judicial justification for the common law's preference for damages has focused on the impact that ordering specific performance may have on the administration of justice. The concern that specific performance is a threat to the administration of justice because of the constant need to supervise and re-litigate the issues must be rejected. The experience of Germany demonstrates that commercial parties prefer an award of damages in the normal case of generic goods or services which are readily available from other providers. However, when specific performance is claimed there are both legal and non-legal mechanisms to ensure that unmeritorious claims are prevented. In this respect a "wait and see" approach should be adopted. If multiple actions do arise the court can revert to damages to bring finality to the dispute. Furthermore, if circumstances change and the parties have not negotiated to vary or discharge the contract, the courts will be able to ensure they can resolve the matter by giving leave to apply for the order to be discharged or varied. Ultimately the decision to risk faulty or delayed performance should be that of the promisee and not the court. Parties who do not want to have their contracts specifically performed in the event of breach can contract out of the presumption, an option not currently open to those who would prefer to contract to have their agreement specifically performed.

The concern that the 'spectre' of contempt of court is inappropriate in contractual disputes fails to explain why cases of specific performance are of particular concern when the court has the same power in other disputes between private parties. In cases where a high level of personal skill or creativity are required, or the order would require the parties to have a personal relationship, specific performance is not appropriate. However, in commercial contracts where the parties are dealing at arms length, the concern that the promisor's liberty will be unjustifiable encroached upon is overstated. Furthermore, it is more appropriate that the promisee is put in the stronger post-breach position than the promisor, who is protected by the primacy of damages. Cases of unwanted performance, where the promisor has no special interest in performing other than the financial profit the transaction will generate, should be prevented and the promisor restricted to claiming damages.

Ordering specific performance for breach of contract vindicates the promisee's decision to enter into the contract. Specific performance is the best method of compensating a promisee for breach of contract because it gives the exact performance bargained for. This protects the promisee's subjective valuation of the performance. Although damages will in many situations satisfy the promisee's interest in performance, it is unsatisfactory that it is for the court to determine what the promisee's best interests are.

Specific performance promotes good faith both in contract formation and in situations where the contract comes to a premature end. Although New Zealand's courts are not bound to order specific

performance in cases under the Sale of Goods (United Nations Convention) Act 1994, it is more appropriate to do so because of the emphasis on performance in the CISG. The frequency of breach will also be reduced because specific performance fosters bargaining. This makes specific performance more efficient and lowers costs. Litigation costs will also be reduced. There will be fewer disputes and the difficult evidentiary issues that currently require determination when calculating damages, and trying to claim that damages are unique, will not arise.

A transitional period will be required to allow both the legal and business communities to adjust to this change in approach. This should not cause undue difficulty, and is justified by the normative and practical advantages of specific performance as the primary remedy for breach of contract. The recommendation is that New Zealand adopts the civil law approach making specific performance the primary remedy for breach of contract.